Quiz 3 Name:____________________________________

Microeconomics - EC 2106

Instructor: Robert McNab Score:________________

INSTRUCTIONS: Please answer all questions to the best of your ability within the allotted time of 10 minutes. You are required to show your work to receive credit. For multiple choice and true/false questions, please circle the appropriate answer. 10 possible points.

1. Which of the following statements is most accurate? 1 point

a. All else remaining equal, if supply increases and demand decreases, price will decline and quantity will increase.
b. All else remaining equal, if supply decreases and demand increases, price will increase and quantity will decrease.
c. All else remaining equal, if supply increases and demand increases, price will be ambiguous and quantity will decrease.
d. All else remaining equal, if supply decreases and demand decreases, price will be ambiguous and quantity will decrease.

2. Assume the market for minivans is in equilibrium. All else remaining equal, if the automobile workers union is able to secure a 10% wage increase, what would happen to the equilibrium price and quantity for minivans. Choose the most accurate answer. 1 point

a. Equilibrium price and quantity would decrease.
b. Equilibrium price would increase and quantity would decrease.
c. Equilibrium price would decrease and quantity would increase.
d. Equilibrium price and quantity would increase.

3. Assume that the market for butter is in equilibrium. All else remaining equal, if the relative price of margarine decreased, what would happen to the equilibrium price and quantity for butter? Choose the most accurate answer. 1 point

a. Equilibrium price and quantity would decrease.
b. Equilibrium price would increase and quantity would decrease.
c. Equilibrium price would decrease and quantity would increase.
d. Equilibrium price and quantity would increase.

4. T F Assume that the price of gold is $325 an ounce in London and $318 an ounce in New York and that transaction costs are equal to 2% of the price per ounce. Is the following statement true or false: There exists sufficient differentiation in price between the two markets that arbitrage would occur. 1 point

5. Assume that the stock of Nike Inc. closed on Friday, February 5, 1999 at $46 a share on a trading volume of 1.18 million shares.. On Saturday, February 6, 1999, an article in Business Week described how consumers under the age of 25 are abandoning major brands like Nike, Levis, and others in favor of relatively unknown brands. At the same time, Nike Inc. stated its intention to spilt its stock so that for every share held on Friday would be equivalent to two shares on Monday. In the space provided below, graphically illustrate what might happen to the equilibrium price and quantity for Nike Inc. stock. 2 points.

6. In your own words, explain the difference in changes in quantity supplied and changes in supply. 2 points.

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7. You have been hired as a consultant for the city of Atlanta and are tasked to provide policy solutions that would help alleviate the low-income housing problem within the city of Atlanta. Using housing data, you determine that the equilibrium rent for 1000 square foot luxury apartments in Buckhead is $1300 a month for 12,500 units rented, while 1,000 square foot luxury apartments near the airport rent for $800 a month for 8,500 units rented. A motion is before the city council to set the maximum rent for 1,000 (or greater) square foot apartments in the city of Atlanta at $850 per month. What policy advise would you offer and how would you back up your conclusions? 2 points (+)

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Quiz 3 Answer Key

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Instructor: Robert McNab

INSTRUCTIONS: Please answer all questions to the best of your ability within the allotted time of 10 minutes. You are required to show your work to receive credit. For multiple choice and true/false questions, please circle the appropriate answer. 10 possible points.

1. Which of the following statements is most accurate? 1 point

All else remaining equal, if supply decreases and demand decreases, price will be ambiguous and quantity will decrease.

2. Assume the market for minivans is in equilibrium. All else remaining equal, if the automobile workers union is able to secure a 10% wage increase, what would happen to the equilibrium price and quantity for minivans. Choose the most accurate answer. 1 point

   Equilibrium price would increase and quantity would decrease.

3. Assume that the market for butter is in equilibrium. All else remaining equal, if the relative price of margarine decreased, what would happen to the equilibrium price and quantity for butter? Choose the most accurate answer. 1 point

   Equilibrium price would decrease and quantity would decrease.

4. **True** Assume that the price of gold is \$325 an ounce in London and \$318 an ounce in New York and that transaction costs are equal to 2% of the price per ounce. Is the following statement true or false: There exists sufficient differentiation in price between the two markets that arbitrage would occur. 1 point

5. Assume that the stock of Nike Inc. closed on Friday, February 5, 1999 at \$46 a share on a trading volume of 1.18 million shares.. On Saturday, February 6, 1999, an article in Business Week described how consumers under the age of 25 are abandoning major brands like Nike, Levis, and others in favor of relatively unknown brands. At the same time, Nike Inc. stated its intention to spilt its stock so that for every share held on Friday would be equivalent to two shares on Monday. In the space provided below, graphically illustrate what might happen to the equilibrium price and quantity for Nike Inc. stock. 2 points.

A stock spilt of 2 for 1 would result in an initial price of \$23 a share and 2.36 million shares (assuming all else remaining equal). This would be represented by an increase in supply.

The article in Business Week represents a change in tastes and preferences among Nike's consumers. This decline in demand for Nike's product will lower individual's expectations for the profitability of

Nike and their demands for Nike stock. This will lead to a decline in demand for Nike's stock. Other explanations are acceptable.

6. In your own words, explain the difference in changes in quantity supplied and changes in supply. 2 points.

Changes in quantity supplied are a direct result of changes in price and represent movements along the supply curve. Changes in supply, on the other hand, are due to other factors (resource costs, number of sells, prices of related producible goods), and represent a shift in the entire supply curve.

7. You have been hired as a consultant for the city of Atlanta and are tasked to provide policy solutions that would help alleviate the low-income housing problem within the city of Atlanta. Using housing data, you determine that the equilibrium rent for 1000 square foot luxury apartments in Buckhead is $1300 a month for 12,500 units rented, while 1,000 square foot luxury apartments near the airport rent for $800 a month for 8,500 units rented. A motion is before the city council to set the maximum rent for 1,000 (or greater) square foot apartments in the city of Atlanta at $850 per month. What policy advise would you offer and how would you back up your conclusions? 2 points (+)

A price ceiling of $850 per month would not affect the market for luxury apartments near the airport since the equilibrium price is below the price ceiling. However, the price ceiling would have an impact in the Buckhead community since the existing equilibrium price is above the proposed maximum price. If a price ceiling was imposed, a <u>shortage</u> would result as the quantity demanded for luxury apartments at $850/per month is greater than the quantity supplied at the same price.

One can illustrate this argument by drawing two separate graphs and illustrating that the price ceiling would have no effect on the market near the airport, while in Buckhead it would result in a shortage. Also, one might note that the reason that the price of apartments is lower near the airport is due to the proximity to the airport (noise, congestion, etc).